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University of Maine System Defined Benefit Pension Fund Annual Report

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DEFINED BENEFIT PENSION FUND
ANNUAL REPORT
YEAR ENDED JUNE 30, 2012

Additional copies are available at <http://www.maine.edu/system/oft/PensionFund.php> or by contacting:

Office of Finance and Administration
16 Central Street
Bangor, ME 04401-5106

Defined Benefit Pension Fund – Annual Report

University of Maine System Year Ended June 30, 2012

The University of Maine System (UMS) Defined Benefit Pension Plan (Pension Plan) is a closed plan, maintained for eligible employees who chose not to join the Defined Contribution Plan established for hourly employees on July 1, 1998. This plan covers a shrinking group of active employees, vested terminated employees, and pensioners.¹

Funded Status of the Pension Plan

The Defined Benefit Pension Plan assets are invested in a separate fund (Pension Fund or the Fund) with assets totaling \$39.9 million at June 30, 2012 compared to \$45.4 million at June 30, 2011. UMS obtains an actuarial valuation every other year. The most recent valuation, completed as of July 1, 2011, showed an Unfunded Actuarial Accrued Liability (UAAL) of \$1.6 million and a funded status of 97%. This compares with a \$2.9 million UAAL on July 1, 2009 and a funded status of 94%.

Oversight and Management

Portfolio and investment management is an ongoing process with the following parties meeting quarterly to provide oversight of Pension Plan assets:

- Board of Trustees Investment Committee
- Investment Consultant – New England Pension Consultants (NEPC) – Cambridge, MA
- Rebecca Wyke, Vice Chancellor for Finance and Administration and Treasurer, UMS
- Tracy Elliott, Director of Finance and Controller, UMS

Governing Guidelines

Formal guidelines, established by the Investment Committee, govern the Pension Fund investment process. These guidelines, last updated August 1, 2011, may be found at <http://www.maine.edu/system/oft/InvestmentGuidelines.php>. They include:

- Total risk and return objectives
- Statement of goals and objectives
- Investment guidelines including
 - Asset allocation with target percentages, permissible ranges, and evaluation benchmarks, and
 - Permitted and excluded investments
- Investment manager performance standards and evaluation
- Responsibilities of all parties
- Conflict of interest statement

¹ For a more detailed history, description and actuarial status of this Pension Plan, see the University of Maine System Annual Financial Report for the Year Ended June 30, 2011, note #13 on Pension Plans which starts on page 49. The financial statements may be viewed at <http://www.maine.edu/pdf/annrpt11.pdf>

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These guidelines currently target a long-term return objective of 7.25% with low to moderate risk. This rate represents a reduction from the 8.0% return objective used during the July 1, 2009 valuation. The 7.25% reflects the lower market return environment.

Fiscal Year 2012 Performance

The markets were volatile and struggled during fiscal year 2012 (FY12). While volatility persists, NEPC advises that emerging market stocks and bonds remain attractive; credit strategies have the highest risk-adjusted expected returns; and lock-up strategies are positioned to harvest attractive liquidity premiums.

The Pension Fund **experienced a return of -0.5%** [-1.1% net of fees] in FY12, placing the Fund in the 83rd percentile (i.e., exceeding 17%) of the total fund universe tracked by the UMS's investment consultant. The UMS return of -0.5% compares to the S&P 500 return of 5.4% and the Barclays Capital Aggregate Bond Index return of 7.5% over the same 1 year period. Performance is a function of market appreciation, asset allocation and the investment managers utilized. The Fund's managers during the fiscal year detracted 110 basis points of value, net of fees. On June 30, 2012, the Fund totaled \$39.9 million, decreasing \$5.5 million over the prior year-end balance as detailed below under the section "Pension Fund Inflows and Outflows".

The Fund's **5-year annualized return was 1.6%** [1.0% net of fees] ranking the Fund in the 64th percentile of the total fund universe (meaning 64% of other funds in the universe performed better) while the risk taken by the UMS Pension Fund was slightly higher compared to other funds in the universe. The UMS 1.6% return compares to the S&P 500 return of 0.2% and the Barclays Capital Aggregate Bond Index return of 6.8% over the same 5 year period.

The Fund is well diversified among a number of asset classes with allocations to eleven investment managers at fiscal year-end.

Changes in Investment Managers and Holdings

Emerging Markets Equity Manager

At its February 2012 meeting, the Investment Committee approved a 5% allocation to emerging markets equity. Aberdeen, an existing manager in the Managed Investment Pool, was approved for the allocation.

High Yield Fixed Income Manager

At its March 2012 meeting, the Board of Trustees approved an allocation to a high yield fixed income strategy. The Investment Committee interviewed firms in May 2012, selecting Loomis Sayles, and approved a 5% allocation to their High Yield Full Discretion Trust product with funds coming from the PIMCO Total Return fund.

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Plan Participants

The Defined Benefit Pension Plan is closed to new participants. Eligible employees who were hired before July 1, 1998 and age 50 or older on June 30, 1998 could elect to roll over their accrued defined benefit to the Defined Contribution Program or remain in the Defined Benefit Pension Plan. Hourly employees hired July 1, 1998 or later participate in the Defined Contribution Program.

Regarding the Defined Benefit Pension Plan, an actuarial valuation is performed every other year. Participant information as of the last two valuations is shown here:

	<u>July 1, 2009</u>	<u>July 1, 2011</u>
Participating Employees ²	106	48
Retirees and Beneficiaries	871	895
Deferred Vested Participants ³	<u>404</u>	<u>381</u>
Total Participants	<u>1,381</u>	<u>1,324</u>

Pension Fund Inflows and Outflows

	(\$ in Thousands)	
	<u>FY11</u>	<u>FY12</u>
Beginning Market Value – July 1	<u>\$42,148</u>	<u>\$45,389</u>
Net External Outflows (e.g., benefit payments and expenses)	(\$4,935)	(\$4,885)
Net Gain or (Loss) on Investments	<u>8,176</u>	<u>(652)</u>
Net Activity for the Fiscal Year	<u>\$3,241</u>	<u>(\$5,537)</u>
Ending Market Value – June 30	<u>\$45,389</u>	<u>\$39,852</u>

Returns, Historical Growth, and Allocation

Attachment I reports the total returns for the Pension Fund on a net of fees basis and the year end market value for the past 5 years, as well as the asset allocation on June 30, 2011 and 2012.

² Shrinking population of those employees who were over age 50 on July 1, 1998 and elected to stay in the Pension Plan. Participating employees includes 19 participants accruing benefits on long-term disability on 7/1/2011 and 29 participants on 7/1/2009.

³ Those who have terminated employment from UMS and are vested but not currently drawing a benefit.

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Market Values, Asset Allocations, and Total Returns

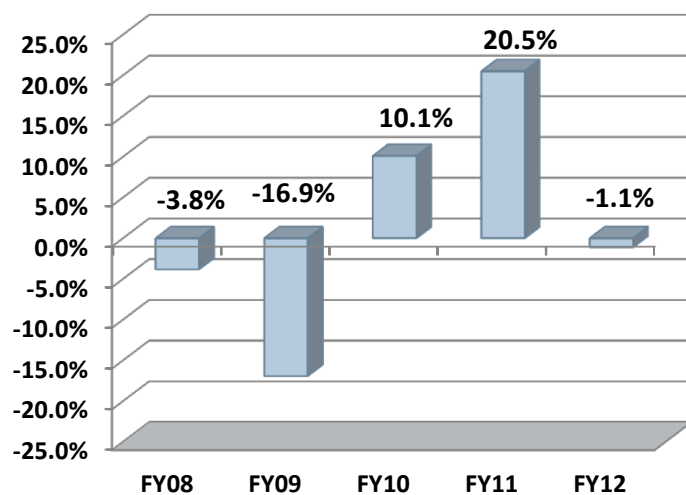
June 30, 2012

Market Value and Asset Allocation of the Defined Benefit Pension Fund (\$ in Thousands)

	June 30, 2011		June 30, 2012	
	Market Value	% Allocation	Market Value	% Allocation
Domestic Equities	\$14,852	33%	\$10,851	27%
International Equities	5,893	13%	6,816	17%
Fixed Income	7,162	16%	7,203	18%
Global Asset Allocation	6,958	15%	6,097	16%
Alternative Investments	7,631	17%	6,775	17%
Core Real Estate	2,474	5%	1,691	4%
Cash	419	1%	419	1%
Total	\$45,389	100%	\$39,852	100%

Total returns (net of fees) and the market value of the Pension Fund for the five years ended June 30, 2012 are shown here:

Total Return (Net of Fees)



Market Value (\$ in Millions)

